In The

Supreme Court of the United States

October Term, 1990

BUSINESS GUIDES, INC.,

Petitioner,

vs.

CHROMATIC COMMUNICATIONS ENTERPRISES, INC. and MICHAEL SHIPP,

Respondents.

On Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

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BRIEF OF RESPONDENTS ON THE MERITS

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QUESTION PRESENTED

Whether the District Court abused its discretion when, pursuant to Federal Rule of Civil Procedure 11, it sanctioned a represented party for filing false evidence in federal district court, having certified with its signature that the evidence was legitimate.

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FEDERAL RULE AT ISSUE

The Federal Rule of Civil Procedure at issue is Rule 11, which provides in pertinent part:

> Every pleading, motion, and other paper of a party represented by an attorney shall be signed by at least one attorney of record in the attorney's individual name, whose address shall be stated. . . . The signature of any attorney or party constitutes a certificate by the signer that the signer has read the pleading, motion, or other paper; that to the best of the signer's knowledge, information, and belief formed after reasonable inquiry it is well grounded in fact and is warranted by existing law or a good faith argument for the extension, modification, or reversal of existing law, and that it is not interposed for any improper purpose, such as to harass or to cause unnecessary delay or needless increase in the cost of litigation. . . . If a pleading, motion, or other paper is signed in violation of this rule, the court, upon motion or upon its own initiative, shall impose upon the person who signed it, a represented party, or both, an appropriate sanction, which may include an order to pay to the other party or parties the amount of the reasonable expenses incurred because of the filing of the pleading, motion, or other paper, including a reasonable attorney's fee.

(As amended Apr. 28, 1983, eff. Aug. 1, 1983).

STATEMENT OF THE CASE[1]

Without inquiring into the validity of what turned out to be false evidence,[2] a national publishing organization accused a tiny competitor of copyright infringement. Business Guides, Inc. ("Business Guides") sought, on sealed papers, a temporary restraining order and permanent injunction to shut down respondent competitor. It also sought $2.25 million in general and punitive damages against Chromatic Communications Enterprises, Inc. ("Chromatic") and its president, Michael Shipp ("Shipp"). Fortunately, the District Court conducted its own inquiry and quickly discovered that the proffered evidence was false. After multiple hearings before a United States Magistrate and pursuant to Rule 11 it dismissed the lawsuit and imposed monetary sanctions of $13,865.66 on Business Guides, an amount equal to Chromatic's attorneys' fees and costs.

Business Guides is a division of New York-based Lebhar-Friedman, Inc., a leading publisher of trade journals and directories, among them the directory of computer and software retailers here at issue. (J.A. 182) Chromatic is a family-run business which in 1986 was operated out of Shipp's garage in Walnut Creek, California, and is now operated out of Shipp's home in Benicia, California. (J.A. 200-201)

[1] Pursuant to Supreme Court Rule 24.2, respondents submit a separate Statement of the Case to correct substantial mischaracterizations of the record in the statement filed by appellant.

[2] Despite sufficient indicia of its false nature, appellant inquired no further. Rather, it simply swore to the accuracy of that which was inaccurate.

In 1986, Chromatic published a directory of computer and software retailers which rivaled Business Guides' directory which sold for about half the price. In 1986 Chromatic sold the printed version of its directory for $247.50, and its diskette version for $595. Business Guides sold its printed version for $389, and its diskette version for $1,125. (J.A. 11-12) Chromatic did not escape the attention of Business Guides or its customers. In fact, the dramatic price difference brought Chromatic to the attention of Business Guides. (J.A. 25, 51) Business Guides learned of the Chromatic directory from its customers, some of whom purchased the Chromatic directory because of the lower price. (J.A. 49) Business Guides watched Chromatic for approximately two years before filing its complaint and application for immediate injunctive relief. (J.A. 51) Asserting that it was motivated to prevent Chromatic from appearing at an important trade show known as Comdex in November, 1986, Business Guides issued a "cease and desist" letter to Chromatic in late October, 1986. (J.A. 46-47, 50)[3]

When Shipp received Business Guides' accusations, he denied copying Business Guides' directory and offered to prove it. (J.A. 124, 128-130, 202-203) Like Business Guides, Chromatic's listings were laboriously compiled using written questionnaires and follow-up research. (J.A. 201) Shipp offered immediately and in writing to show his questionnaires and other research papers to Business Guides because they prove that all of the entries in the

[3] Ironically, Shipp never planned to participate in the 1986 Comdex show, a fact about which appellant never inquired.

Chromatic directory were a result of Shipp's own independent industry. Instead of taking the opportunity to examine these records, however, appellant filed this suit almost immediately on October 31, 1986. To support its application for a temporary restraining order and permanent injunction against Chromatic, appellant not only declined to check Shipp's records, it neglected to check its own, even though it had two years to prepare its case.

Business Guides has substantial experience in litigating infringement suits (J.A. 105-106, 112) and boasts of being one of the pioneers in using so-called "seeds" to detect infringers. Business Guides, like many publishers of directories, "seeded" its directory with false information. Seeds consisted of totally fictitious entries (Type A Seeds) or legitimate entries which contained intentional errors, such as misspellings or incorrect telephone numbers or addresses (Type B Seeds). A record of the seeds was compiled in a Master Seed List. Business Guides avers and Chromatic does not dispute that the practice of using seeds in directories is a common industry practice undertaken for the sole purpose of catching infringers.

Business Guides claimed that out of the "thousands of business listings laboriously compiled" and hundreds of thousands of bits of information, Chromatic copied a total of only ten. Nine were so-called "Type-B" seeds and one was a so-called "Type A" seed. Business Guides presented this evidence by declaration of its Director of Research, Michael Lambe, who was directly in charge of its seeding operation and copyright enforcement.[4]

[4] Appellants, alternately refer to Mr. Lambe as a "junior employee" (Appellant's brief 10), and a "mid-level employee"

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The significance of the seeds was not readily apparent to the District Court and The Hon. Samuel Conti's law clerk asked counsel for Business Guides to explain how the purported seeds were evidence of copying. (J.A. 121) Prompted by the Court's inquiry, appellant prepared a supplemental declaration and in the process attempted to verify the ten seeds. Mr. Lambe then conducted a cursory investigation of "easily verifiable" seeds. (J.A. 187) He briefly consulted a zip code directory and past Business Guides directories. In a matter of minutes, Mr. Lambe discovered that four of the ten seeds were indeed invalid, but inquired no further. (J.A. 187-189) Instead of verifying the remaining six, he submitted a supplemental declaration which excluded the invalid seeds but resubmitted the remaining six, unverified seeds. Remarkably, even though Chromatic had been "under investigation" by Business Guides for two years, Business Guides claims that it did not have time to verify the remaining seeds.

Understandably suspicious about the deletion of some of the seeds, and wary because Chromatic was excluded from reviewing and responding to the sealed papers, the District Court investigated the remaining seeds by telephoning the subject businesses. The Court then found that eight out of the ten listings contained

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(Appellant's brief 34, n.38). The objective facts establish that he had thirteen years of experience at Business Guides, was in charge of preparing the seed list, had the authority to institute litigation, and in fact had brought and won at least one previous infringement suit against Xerox Corp. (J.A. 53,187)

correct information about legitimate businesses, and were therefore not seeds. (Pet.App. 66a) The Court's investigation took under an hour. (Pet.App. 56a) The Court denied the Application for a Temporary Restraining Order and referred the case to the United States Magistrate for evidentiary hearings into the appellant's submission of false evidence.

The proceedings before the magistrate were conducted in camera, and Chromatic was not permitted to participate. Chromatic later learned that Business Guides offered a different explanation for the false seeds at each hearing. The Magistrate found the explanations proffered at the first two hearings preposterous. (Pet.App. 68a,71a) After those first two hearings, the Magistrate concluded that Business Guides failed to conduct the reasonable inquiry required by Rule 11 and also that it intentionally tried to cover up its failure by fabricating excuses before the Magistrate. (Pet.App. 73a)

At the third hearing, Business Guides admitted that its prior explanations to the Magistrate as to why the seeds were not seeds were not credible. It claimed that until its current counsel unraveled the puzzle of the faulty seed list, Business Guides could not explain why it contained erroneous seeds, even though Business Guides, not counsel, prepared the list. The record, however, suggests that even the third explanation is less than reliable.

Contrary to the assertion in appellant's brief that Mr. Lambe did not participate in the preparation of the seed list (Appellant's brief 10), Michael Lambe was Director of Research and in charge of the seeding process. Furthermore, Mr. Lambe stated in a declaration that he and

another Business Guides employee "forgot" that *they* used an unusual process in preparing these particular seeds. Suddenly in January 1987 they "remembered" the circumstances of their preparation. (J.A. 192) At the conclusion of a third evidentiary hearing, the Magistrate revised his report. He still recommended that both Business Guides and its counsel[5] be sanctioned under Rule 11 for failing to make a reasonable inquiry prior to filing suit. Contrary to Business Guides' continued refrain (Appellant's brief p. 15), the Magistrate never affirmatively found that Business Guides acted in good faith. Rather, the Magistrate merely concluded that he no longer believed that appellant had engaged in an intentional cover-up. (Pet.App. 48a)

Thereafter, the Court invited Chromatic to move for sanctions. (*Business Guides v. Chromatic Communications Enterprises Inc. and Michael Shipp,* 119 F.R.D. 685 (N.D. Cal. 1988) (reprinted at Pet. App. 35a-46a.) In April 1988, approximately eighteen months after this suit was filed against it, the Court unsealed the record and Chromatic was able to view the evidence offered against it. Chromatic discovered that the solitary Type A Seed listed by Business Guides, "NFR Computer Room," was planted in its directory by Business Guides itself. (J.A. 200-209). Had

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[5] Before the sanctions motion could be heard, counsel for Business Guides, Finley, Kumble, Wagner, Heine, Unterberg, Manley, Myerson & Casey ("Finley Kumble") filed for bankruptcy protection. By Order of the Bankruptcy Court, Chromatic withdrew its Motion for Sanctions as to Finley Kumble. Chromatic firmly believes that counsel's conduct violated Rule 11 and would not have withdrawn its Motion voluntarily as appellant insinuates. (See, e.g., Appellant's brief at p. 17)

Business Guides accepted Shipp's invitation to examine Chromatic's records, it would have found in Chromatic's files the NFR Computer Room questionnaire completed by a Business Guides employee. (J.A. 208-209; Pet. App. 29a-31a)

The only remaining seed was a Type B seed, a single misspelling of a man's name. Business Guides asserted that the proper spelling of the name was "Choi" but that it had intentionally misspelled it in its directory as "Choy." (J.A. 87, 190) Business Guides' entire lawsuit seeking, *inter alia*, an accounting, impoundment, $750,000 in general damages, $1.5 million in punitive damages, and endeavoring to put Chromatic out of business, rested on Chromatic's coincidental misspelling of the name as "Choy." Simply stated, the entire lawsuit hung on the evidence that, out of the thousands of listings and hundreds of thousands of pieces of information in the directory, Chromatic misspelled one name by using its most common spelling.

The District Court sanctioned Business Guides for failing to make a reasonable inquiry into its evidence before filing it with the Court. Given that after three evidentiary hearings its infringement claim proved to be utterly without merit, the Court likewise imposed the terminating sanction of dismissal. *Business Guides v. Chromatic Communications Enterprises, Inc. and Michael Shipp*, 121 F.R.D. 402 (N.D. Cal. 1988) (reprinted at Pet. App. 27a-34a, at 34a).

Relying on most of the same arguments presented here, Business Guides appealed. A unanimous panel of the Ninth Circuit Court of Appeals affirmed. *Business Guides v. Chromatic Communications Enterprises, Inc., et al.*,

892 F.2d 802 (9th Cir. 1989). Unrepentant, Business Guides now seeks this Court's sympathy for the inconvenience it has withstood throughout the appellate process. It shows no sympathy, however, for the plight of Chromatic, which, after having been wrongfully accused nearly four years ago, remains embroiled in pointless litigation. To follow the plain meaning of Rule 11 and carry out its purpose, the decision of the Court of Appeals for the Ninth Circuit should not be disturbed.

SUMMARY OF ARGUMENT

Chromatic opposed Business Guides' Petition for Certiorari on the ground that Business Guides' conduct is deserving of sanctions regardless of whether an objective or subjective standard is applied. The objective standard, however, is the one mandated by the plain meaning of the Rule and best carries out its objectives. In addition, the double standard proposed by Business Guides is unworkable and unnecessary.

First, the plain meaning of Rule 11 establishes an objective reasonableness standard for the imposition of sanctions for its violation. The Rule does not differentiate between attorneys, the parties they represent, or pro se litigants. Nothing in the language of Rule 11 supports the spontaneous injection of a double, or second, standard of conduct for represented parties and for no one else. Rather, the very terms of the Rule provide that whether it is violated, and by whom, is judged according to whether the conduct is reasonable under the circumstances of the

case. Moreover, the 1983 Amendments to Rule 11 expressly deleted the "good faith" defense.

Second, applying a uniform objective standard best promotes the central purpose of deterring frivolous lawsuits without prompting satellite litigation or chilling vigorous advocacy of legitimate claims. To apply different standards to different players in litigation confuses what is and what is not sanctionable conduct. Injecting variable standards only lengthens the inquiry and requires protracted discovery and satellite proceedings. In addition, the 1983 amendments to Rule 11 were expressly intended to encourage courts to impose sanctions, a goal better accomplished by application of a predictable, uniform standard.

Third, the double standard proposed by Business Guides is unworkable and unnecessary. It is unworkable because the application of a separate standard would require a lengthy inquiry into subjective intent. Such an inquiry would prolong proceedings, collide with the attorney-client privilege and inevitably erode the attorney-client relationship. It is unnecessary because courts have the inherent power to sanction bad faith conduct. *Newman v. Piggie Park Enterprises, Inc.*, 390 U.S. 400, 402 n.4, 19 L.Ed.2d 1263, 1266 (1968).

Fourth, regardless of which standard is applied, Business Guides violated the Rule. After watching Chromatic for two years, it blindly rushed into litigation without investigating the facts upon which its purported copyright infringement claim was based. Moreover, Business Guides declined an opportunity to examine Chromatic's

records. Instead of devoting a few hours to reviewing respondent's records to determine whether or not its accusations had any basis in fact, it spent 99 hours preparing its pleadings and application for a temporary restraining order. (J.A. 102) After initiating litigation, when the district court alerted Business Guides to errors in its evidence, it did not withdraw its suit. Even after its own inquiry revealed that its evidence was not reliable, it failed to investigate further.

A reasonable litigant in Business Guides' circumstances would have eagerly examined Chromatic's records and would certainly have examined its own before swearing under penalty of perjury that a small competitor had stolen its work. Business Guides conducted none of these pre-filing inquiries, and the facts support a finding that it failed to do so because of its ambition to squash a competitor, regardless of whether the competitor had copied its directory. This is not a case in which a party was slapped with monumental sanctions for an innocent error, in spite of appellant's attempt to characterize it as such. Rather, this is a case in which the Court imposed modest sanctions against the party whose cavalier review of the facts led to the filing of a frivolous and utterly meritless lawsuit. Business Guides' failure to inquire cast a four-year pall over Chromatic's business, and needlessly consumed Court time more justly devoted to legitimate disputes. Under a subjective or objective standard, Business Guides violated Rule 11 and was properly sanctioned.

ARGUMENT

A. The Plain Language And Purpose Of Rule 11 Mandate A Uniform, Objective Standard

Asserting that subjective good faith protects represented parties from the consequences of their Rule 11 violations injects into the Rule provisions that are neither stated nor contemplated, and which run counter to its central purpose: to deter the filing of groundless lawsuits. The standard more consistent with Rule 11's language and purpose, and the one supported by the vast weight of circuit authority, is that violations be judged by a uniform, objective standard of reasonableness.

1. The Plain Language of Rule 11 Does Not Accommodate the Proffered Double Standard

In the first instance, Federal Rule 11, as any statute, must be interpreted according to its plain meaning. *Pavelic and LeFlore v. Marvel Entertainment Group*, ___ U.S. ___, 110 S.Ct. 456, 107 L.Ed.2d 438 (1989). See also, Justice F. Frankfurter, *Some Reflections on the Reading of Statutes*, 47 Colum.L.Rev. 527 (1947). When the Court finds the terms of the rule or statute unambiguous, the judicial inquiry is complete. *Pavelic*, quoting *Rubin v. U.S.*, 449 U.S. 424, 430, 66 L.Ed.2d 633, 638 (1981).

The plain language of Rule 11 expressly states that it applies to attorneys, pro se litigants, and represented parties.[6] When any of the actors signs a paper filed in a

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[6] Rule 11 states:

The signature of an attorney or party constitutes a certificate by the signer that the signer has read the

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federal court, the signer – an attorney, represented party or pro se litigant – certifies that it is well-grounded in fact, based on a reasonable inquiry. If the Rule is violated, sanctions are mandatory. Fed. Rule Civ. Pro. 11, Notes of Advisory Committee on Rules, 1983 Amendment (West. 1990) (hereafter "Advisory Committee Notes"); *Chevron, U.S.A., Inc. v. Hand*, 763 F.2d 1184,1187 (10th Cir. 1985) It is thus not merely a "standard of professional competence" applicable to members of the legal profession, as asserted disingenuously (and frequently) by appellants. Rather, it is a powerful and essential means of controlling litigation and the conduct of participants in the federal judicial system. *Cooter and Gell v. Hartmarx Corp.*, ___ U.S. ___, 110 S.Ct. 2447, 110 L.Ed 2d 359 (1990).

The Rule establishes an affirmative and mandatory duty of "reasonable inquiry" by the person signing a

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pleading, motion or other paper; that to the best of the signer's knowledge, information and belief found after reasonable inquiry, is well grounded in fact and is warranted by existing law or a good faith argument for the extension, modification or reversal of existing law, and that it is not interposed for any improper purpose, such as to harass or to cause unnecessary delay or needless increase in the cost of litigation . . . if a pleading, motion, or other paper is signed in violation of this rule, the court, upon motion or upon its own initiative, shall impose upon the person who signed it, a represented party or both an appropriate sanction which may include an order to pay to the other party or parties the amount of reasonable expenses incurred because of the filing of the pleading, motion or other paper, including a reasonable attorney's fee.

paper filed in federal court, both as to the veracity of its contents *and* as to the propriety of its purpose. Thus, the Rule is violated *either* if the signer has not conducted a reasonable inquiry *or* if the signer files the paper for an improper purpose, or both. See, e.g. *Townsend v. Holman Consulting Corp.*, ___ F.2d ___, 90 Daily Journal D.A.R. 9995, 9996 citing *Zaldivar v. City of Los Angeles*, 780 F.2d 823, 832 (9th Cir. 1986). Moreover, the Rules Advisory Committee observed, "If the duty imposed by the Rule is violated, the Court should have the discretion to impose sanctions on either the attorney, the *party* the attorney represents, or both . . . and the new rule so provides." Advisory Committee Notes (emphasis added). While Rule 11 readily recognizes that a represented party may be a target of sanctions, the Rule does not include any provision for a separate standard by which to judge a represented party's conduct. Yet Business Guides urges this Court to rewrite Rule 11 to allow sanctions against represented parties only where they *both* failed to conduct a reasonable inquiry *and* were motivated by subjective bad faith.

The plain language of Rule 11 simply does not accommodate appellant's strained interpretation. In fact, the Advisory Committee on the Rules[7] underscored that the 1983 amendments to Rule 11 specifically abandon the "good faith" formula for a more stringent standard. See *Eastway Construction Corp. v. City of New York*, 762 F.2d 243, 253 (2d Cir. 1985) *cert. denied*, 484 U.S. 918, 98

[7] Committee reports carry great weight in interpreting a statute. *Garcia v. United States*, 469 U.S. 70, 76, 83 L.Ed.2d 472, 478 (1984).

L.Ed.2d 226 (1987) ("Simply put, subjective good faith no longer provides the safe harbor it once did.") The Advisory Committee also noted that the more stringent standard was adopted expressly to encourage courts to impose sanctions. Advisory Committee Notes. Moreover, commentators recognize that the subjective bad faith element was abandoned with the 1983 Amendments because it proved to be "a virtually unattainable standard." A. Miller, *The New Certification Standard Under Rule 11*, 130 F.R.D. 479, 482 (1990).

Rule 11, as written, amended and interpreted in the vast majority of the federal circuits, unequivocally establishes an affirmative duty on counsel, parties, and pro se litigants alike to inquire into the facts and the law before filing. To determine whether that duty is fulfilled, the standard embraced by commentators and applied in the majority of circuits is one of reasonableness under the circumstances. Advisory Committee Notes. Miller, *Certification Under Rule 11*, at 483 ("The sufficiency of the signer's inquiry is tested against a standard of reasonableness under the circumstances. The standard is more objective and therefore more demanding . . . "); *Gaiardo v. Ethyl Corp.*, 835 F.2d 479 (3rd Cir. 1987) ("The Rule imposes an obligation on counsel and client analogous to the railroad crossing sign, 'Stop, Look and Listen.' It may be rephrased, 'Stop, Think, Investigate and Research' before filing papers either to initiate a suit or to conduct the litigation"); *Kale v. Combined Ins. Co. of America*, 861 F.2d 746, 757 (1st Cir. 1988); *Cleveland Demolition Co. v. Azcon Scrap Corp.*, 827 F.2d 984, 987-88 (4th Cir. 1987); *Thomas v. Capital Securities Services, Inc.*, 836 F.2d

866, 870 (5th Cir. 1988); *INVST Financial Group, Inc. v. Chem-Nuclear Systems, Inc.*, 815 F.2d 391, 401 (6th Cir. 1987) *cert denied, sub nom Garratt v. INVST Financial Group, Inc.*, 484 U.S. 927, 98 L.Ed.2d 251; *In re Ronco, Inc.*, 838 F.2d 212, 217 (7th Cir. 1988) quoting *Colan v. Cutler-Hammer, Inc.*, 812 F.2d 357, 360 n.2 (7th Cir. 1987), *cert. denied*, 484 U.S. 820 ("The test under Rule 11 is objective: litigation must be grounded in an objectively reasonable view of the facts and the law and, if it is not, the lawyer or party proceeding recklessly must foot the bill."); *O'Connell v. Champion International Corp.*, 812 F.2d 393 (8th Cir. 1987); *Zaldivar v. Los Angeles*, 780 F.2d 823 (9th Cir. 1986); *Adamson v. Bowen*, 855 F.2d 668 (10th Cir. 1988).

Business Guides, through its Director of Research, signed declarations setting forth its purported evidence of copyright infringement and thereby certified that it had conducted a reasonable inquiry into those facts, when it had not. It failed entirely to conduct any inquiry before initiating a lawsuit seeking over a million dollars in damages and with the potential and intent of putting a small competitor out of business. It failed to conduct a reasonable inquiry even after the small portion of the evidence it checked proved unreliable. Regardless of its good faith or bad faith, Business Guides violated Rule 11 and was justly sanctioned.

2. Rule 11's Central Goal of Deterrence Is Best Achieved by a Single, Objective Standard

The central purpose of Rule 11 is to deter the filing of groundless lawsuits. Although the Rule must be read in light of the secondary concerns that it will spawn satellite

litigation and chill vigorous advocacy, "any interpretation must give effect to the rule's central goal of deterrence." *Cooter & Gell v. Hartmarx Corp.*, ___ U.S. ___, 110 S.Ct. 2447, 110 L.Ed 2d 359, 374 (1990).[8]

A rule that is applied uniformly and predictably is more likely to deter frivolous suits than one which is applied erratically and unevenly. If the goal is to rid the federal judicial system of frivolous lawsuits, then the rule must sanction all those whose conduct caused them to be filed. *Pavelic & LeFlore*, 107 L.Ed.2d at 445; See, A. Untereiner, *A Uniform Approach To Rule 11 Sanctions*, 97 Yale L.J. 901, 915 (1988).

Business Guides argues that sanctions should not have been imposed because a requirement of subjective bad faith should be read into the duty of reasonable inquiry when applied to a represented party. To judge the conduct of attorneys and pro se litigants by an objective standard while applying the more lenient subjective standard to parties represented by counsel establishes a double standard of conduct. That double standard proposed by Business Guides would provide a safe harbor for a represented party from liability under Rule 11, so long as its opponent could not affirmatively establish bad faith.[9]

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[8] The vast majority of circuit courts embraced the objective standard even before this Court in, *Cooter & Gell*, unequivocally established deterrence as the Rule's primary goal.

[9] Here, of course, Chromatic and Shipp were not allowed to participate in the hearings, and thus were given no opportunity to demonstrate such bad faith. The use of a subjective standard in such a circumstance denies the excluded party its due process right to protect its interests.

Such a standard would do more to encourage than deter frivolous lawsuits. As the Ninth Circuit recently observed, "It would ill serve the purpose of deterrence to allow . . . a 'safe harbor' for improper or unwarranted allegations." *Townsend v. Holman Consulting Corp.*, ___ F.2d ___, 90 Daily Journal D.A.R. 9995, 9997 (9th Cir. Sept. 7, 1990). Providing a safe harbor to a large corporation with substantial resources such as Business Guides would do nothing to deter it from filing groundless lawsuits. Rather, it may encourage it to risk sanctions by hastily filing suit in order to push a small competitor with limited resources, such as Chromatic, out of business.

Even if Business Guides acted without bad faith, its so-called "mistake" dragged Chromatic and Shipp into court, has kept the small company under a cloud for four years, and has consumed innumerable hours of court time. Under the circumstances, even if both parties are innocent, and appellant plainly is not, it should be Business Guides which is held accountable for the resultant costs. To hold otherwise is to victimize Chromatic and Shipp still further.

3. A Subjective Bad Faith Standard Impermissibly Complicates and Protracts Rule 11 Proceedings

A single, objective standard best meets Rule 11's foremost goal of deterrence without generating satellite litigation or chilling vigorous advocacy. To avoid protracted satellite proceedings, the Advisory Committee cautioned that sanctions proceedings should be limited to the record already established in the case. Here, the District Court was far more lenient: before recommending

sanctions the District Court reviewed carefully Business Guides' evidence and allowed three evidentiary hearings. Chromatic, as noted, was prevented from participating in the evidentiary hearings.[10] As a result, the record in this case is largely composed of documents prepared and testimony given by Business Guides' employees on behalf of Business Guides. Chromatic had no opportunity to cross-examine witnesses or impeach evidence. Despite the absence of one party, two violations were found, and sanctions imposed.

If, to recover sanctions under Rule 11, Chromatic must establish Business Guides' subjective bad faith, Chromatic would be entitled to discovery, and a due process right to be heard. Permitting discovery, and the host of procedures, abuses, and enforcement devices that commonly accompany it, would inevitably protract the sanctions proceedings. Ultimately, the sanctions proceedings would evolve into a lawsuit within the original lawsuit and impede Rule 11's goal of imposing sanctions without creating satellite litigation. Rather than encouraging courts to impose sanctions, the cumbersome, time-consuming procedure would discourage parties from

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[10] Had it been allowed to participate, it would have proven that the sole Type A Seed was planted in its directory by Richard Rossini, a Business Guides employee whose declaration swears that the listing was fictitious, and could only have appeared in respondents' directory through copying. The record is now clear, and the District Court found on the basis of uncontroverted evidence, that respondents obtained that listing because Mr. Rossini both ordered Chromatic's directory and completed its questionnaire in the name of that fictitious business. It is hard to consider Mr. Rossini's Declaration anything other than a blatant lie, and another violation of Rule 11, subjectively or objectively.

seeking sanctions and courts from imposing them. The language, and intent of Rule 11 is to the contrary.

It is difficult to understand how imposing sanctions for Business Guides' conduct absent an affirmative finding of its bad faith would chill vigorous advocacy of legitimate claims. Commentators have recognized the potential of Rule 11 to cool the zeal of attorneys to accept and argue novel or unpopular causes of action. See, M. Nelken, *Has The Chancellor Shot Himself In The Foot? Looking For A Middle Ground On Rule 11 Sanctions*, 41 Hastings L.J. 383, at 393 (1990). Business Guides, however, presented no novel approach to the law. Rather, Business Guides failed entirely to meet the Rule 11 reasonable inquiry requirement, and as a result of that failure filed false "evidence" in support of an utterly meritless lawsuit seeking immediate injunctive relief against and $2.25 million in damages from a competitor. This is not an instance in which legitimate advocacy was unjustly squelched; rather, this was precisely the conduct Rule 11 is intended to prevent.

4. A Double Standard of Conduct Is Unworkable and Unnecessary

Application of a double standard, that is, a subjective standard of conduct for represented parties and an objective standard of conduct for everyone else, clearly contravenes the plain language of Rule 11, its purpose, and well-settled principles of statutory interpretation. Moreover, such dual standards are unworkable and unnecessary.

The double standard is unworkable because it impermissibly and unwisely complicates the Rule 11 inquiry, thereby increasing the cost of litigation both to the judicial system and to litigants. Before any conduct could be evaluated, the initial Rule 11 inquiry would begin with a determination of whether the target of Rule 11 sanctions was an attorney, the client, or both.

Separate proceedings, on separate standards would be required and would inevitably consume more time and expense than application of a uniform objective standard.[11] Ultimately, such burdens would discourage courts and parties from invoking the Rule except in the most egregious circumstances, a result directly contrary to the intention of the 1983 amendments to the Rule.

Moreover, the proffered double standard is unnecessary; if the Rule's goal had been to authorize the assessment of fees only for bad faith litigation conduct, no new statutory provision would have been necessary. The federal courts have long had equitable power to award counsel fees for bad faith or oppressive tactics. *Newman v. Piggie Park Enterprises, Inc.*, 390 U.S. 400, 402, n.4; 19 L. Ed 2d, 1263, 1266 (1968); *Christianburg Garment Co. v. Equal Employment Opportunity Commission*, 434 U.S. 412, 54 L.Ed 2d, 648 (1978). The amended Rule was intended to build upon and expand the court's equitable power to award sanctions for bad faith conduct. Advisory Committee

[11] Furthermore, such dual proceedings would implicate the attorney-client privilege in nearly every proceeding and would create serious conflicts between counsel and his or her client.

Notes. Requiring a showing of bad faith would curtail rather than expand the scope of the Rule.

B. A Uniform Standard Of Objective Reasonableness Comports With Federal Rules And Common Law Duty Of Care

1. No Other Federal Rule Applies a Double Standard

Uniform application of a single standard of conduct is consistent with the interpretation of other federal procedural rules. Injecting a double standard of conduct under Rule 11 would subvert the intent and, in effect, revise the application of other federal rules.

For example, Rule 26(g) authorizes the imposition of sanctions for discovery abuses, and closely parallels the signing and certification requirements of Rule 11. It states that the signature of the attorney *or party* constitutes a certification that the *signer* has read the document and that to the best of the signer's knowledge, information and belief formed after a *reasonable inquiry*, it is legitimate. Like Rule 11, Rule 26(g) encourages the imposition of sanctions for abuse. The Notes of the Advisory Committee on Rule 26 observe that the duty to make a reasonable inquiry under Rule 26 is judged by an objective standard. The Committee does not suggest that a distinct standard should apply to represented parties. Advisory Committee Note to Rule 26(g).

Similarly, Federal Rule of Civil Procedure 37 allows the imposition of sanctions against parties and counsel for discovery abuses. See, e.g. *Farm Construction Services Inc. v. Fudge*, 831 F.2d 18 (1st Cir. 1987); *Chapman & Cole v. Itel Container Int'l*, 865 F.2d 676 (5th Cir. 1989), *cert. denied*, ___ U.S. ___, 110 S.Ct. 201, 107 L.Ed.2d 155 (1989). It contains no requirement of subjective bad faith.

Rule 16(f) provides that if a party or party's attorney fails to obey a scheduling or pretrial order, sanctions may be appropriate. Rule 16(f), like Rule 11, expressly provides for imposing sanctions on disobedient or recalcitrant parties, their attorneys, or both, without imposing a separate standard of conduct. Notes of Advisory Committee on Rule 16. (West 1990).

Again, under Rule 38 of the Federal Rules of Appellate Procedure, which provides for sanctions for frivolous appeals, courts have applied a single standard. A single uniform and objective standard considers the individual circumstances of the case, including, where appropriate, the status of the individual signer, whether an attorney, a represented party or a pro se litigant. The framers of Rule 38 did not establish an entirely new and unwritten standard for represented parties. See, e.g., *Clarion Corp. v. American Home Products Corp.*, 494 F.2d 860, 866 (7th Cir. 1974), *cert. denied*, 419 U.S. 870; *Wood v. McEwen*, 644 F.2d 797 (9th Cir. 1981), *cert. denied*, 455 U.S. 942 (1982); *Ruderer v. Fines*, 614 F.2d 1128 (7th Cir. 1980); *Clark v. Green*, 814 F.2d 221, 223 (5th Cir. 1987). This Court should not do so now with respect to Rule 11.

2. As Applied in Negligence Law, Objective Standard Encompasses Circumstances Relevant to Party's Conduct

The objective standard as applied to conduct under the federal rules is the same as that applied under general

negligence and professional liability law – that of objective reasonableness under the circumstances. Business Guides argues that it is unfair to apply the objective reasonableness standard to parties in Rule 11 cases because it establishes a "standard of professional competence" for lawyers. As noted previously (at p. 13), the Rule is a means of controlling litigation in federal courts, not singularly a tool for disciplining lawyers. Nor should it become one.

As applied, the objective standard does not impose the virtual strict liability implied by appellants. Rather, the reasonableness standard takes into account factors relevant to evaluation of the alleged violation. Those factors include consideration of whether the litigant is a party, an attorney, or a pro se litigant, just as the common law negligence standard of care takes into account circumstances peculiar to the defendant, such as a mental disability, or professional qualifications or training. See, e.g. *Huffman v. Lindquist*, 37 Cal.2d 465, 473 (1951) (the standard applied to physicians "demands that a physician or surgeon have the degree of learning and skill ordinarily possessed by practitioners of the medical profession in the same locality . . . "); Rest. 2d Torts, § 289, Comment n (A professional is required to make reasonable use of superior knowledge, skills and experience within the area of expertise.)

The objective reasonableness standard encompasses all appropriate and relevant variables, including, for example, Business Guides' familiarity with the litigation process. Its argument that it is unjust to apply the same standard to lay persons rings hollow. Neither reason nor

precedent supports applying the unique double standard to judge conduct under Rule 11.

C. Even Under The Second Circuit's Standard, Business Guides Violated Rule 11

Business Guides urges the adoption of the standard of conduct articulated by the Court of Appeals for the Second Circuit in an attempt to exonerate itself from Rule 11 liability. Even under the Second Circuit approach, however, Business Guides violated the Rule.

Business Guides places primary reliance on *Calloway v. Marvel Entertainment Group*, 854 F.2d 1452 (2d Cir. 1988), reversed in part *sub nom* on other grounds, *Pavelic & LeFlore v. Marvel Entertainment Group*, ___ U.S. ___, 107 L.Ed.2d 438, 110 S.Ct. 456 (1989).[12] Business Guides argues that *Calloway* supports its proposition that a subjective "bad faith" standard should be applied when a represented party is the target of Rule 11 sanctions, and that if that standard had been applied, Business Guides would not have been sanctioned. *Calloway* does not mandate such a conclusion. In *Calloway*, the Second Circuit purported to apply a subjective test to determine whether

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[12] This issue is not the first one regarding Rule 11 upon which the Second Circuit found itself isolated and ultimately reversed by this Court. The Second Circuit ruled that a voluntary dismissal acts as a jurisdictional bar to Rule 11 proceedings in *Johnson Chemical Co., Inc. v. Home Care Products, Inc.*, 823 F.2d 28,31 (2d Cir. 1987). This Court decided the opposite in *Cooter & Gell v. Hartmarx Corp.*, ___ U.S. ___, 110 L.Ed.2d 359, 375 (1990). Chromatic suggests that the Second Circuit's imposition of a double standard is also a maverick view appropriate for reversal.

a party, ostensibly represented by counsel, violated the Rule. *Calloway* is distinguishable on its facts. The party, Mr. Calloway, besides being unrepresented in the appeal, was mentally ill and had such a tenuous grip on reality that the Court was loathe to hold him to an objective standard of reasonableness. Of course application of an objective standard with recognition of his mental incapacity would likewise result in his exoneration from sanction liability.

The Second Circuit cases following *Calloway* cited by appellants also miss the point. In *Greenberg v. Hilton International Company*, 870 F.2d 926 (2d Cir. 1989), the represented party was the target of Rule 11 sanctions in a Title VII action for gender discrimination. Although the plaintiff had a prima facie case when the suit was filed, subsequent precedent rendered her claim meritless. All of the papers filed in *Greenberg* were signed by the attorney, and not by the party. Thus, the real issue in *Greenberg* was not what standard should be applied to judge a represented party's conduct, but whether a represented party should be sanctioned under Rule 11 for the conduct of counsel in filing a lawsuit which subsequently proved to be *legally*, rather than factually, insufficient. *Greenberg* is markedly distinct from the case here, where Business Guides itself signed the declarations[13] under oath swearing to facts solely within the party's knowledge, expressly not matters solely within its attorney's expertise.

Similarly, in *Cross & Cross Properties, Ltd. v. Everett Allied Company*, 886 F.2d 497 (2d Cir. 1989), the defendant

[13] The declarations include two by Mr. Lambe and one by Mr. Rossini.

sought sanctions against a party for filing a meritless cross-complaint in complex litigation regarding a tax shelter. Again, all papers were signed by counsel. The Second Circuit held that while Rule 11 sometimes allows sanctions against a client even if he does not sign the pleadings, sanctions may not be directed against a represented client without a showing that a client has actual knowledge that filing the paper constituted wrongful conduct. *Cross & Cross* at 505, citing *Calloway* at 1474 and *Greenberg* at 939.

The standard applied in the above cases would not excuse Business Guides' conduct. Unlike *Calloway*, Business Guides was not a mentally ill novice to the legal arena. Rather, Business Guides generally, and Mr. Lambe in particular, were pioneers in copyright infringement litigation with significant familiarity with the process. See, e.g., *Chain Store Business Guides, Inc. v. Wexler*, 79 F.Supp. 726 (S.D.N.Y. 1948). Unlike parties in *Greenberg* and *Cross & Cross*, Business Guides was sanctioned for itself signing documents swearing to facts within its own knowledge and expertise, not for counsel's certification of legal argument or analysis.

Appellant cites no cases in which a represented party was exonerated from sanctions under Rule 11 for filing false evidence under the defense that it was an honest mistake. In *Calloway* and its progeny, the parties were relatively nonculpable. Business Guides' conduct, however, would support a finding of bad faith under the *Calloway* standard.

Business Guides is a self-styled expert in enforcing its copyrights and claims to have investigated Chromatic

for two years. Suddenly, when its customers started buying Chromatic's product, Business Guides launched into litigation without adequately inquiring into whether it had grounds to do so. After the Hon. Samuel Conti's law clerk alerted Business Guides to its own inquiry into the evidence, Business Guides discovered that four out of ten seeds were false. A reasonable litigant with thirteen years of similar experience should have inquired further. It is impossible to believe that Mr. Lambe, whose job it was to oversee preparation of the seeds, did not harbor severe misgivings as to the accuracy of the seeds. He either knew they were false or recklessly relied on their trustworthiness.

These circumstances are enough to satisfy the actual malice standard in the analogous area of defamation law. It can constitute actual malice if, when faced with obvious reasons to doubt the veracity or trustworthiness of information, an individual fails to inquire further before publishing it. See e.g. *St. Amant v. Thompson*, 390 U.S. 727, 732, 20 L.Ed.2d 262, 268 (1968), citing *Curtis Publishing Co. v. Butts*, 388 U.S. 130, 170, 18 L.Ed 24 1094, 1119 (1967). If Business Guides can escape sanctions for recklessly, if not knowingly, filing false declarations swearing to non-existent evidence, when it had obvious reasons to doubt its accuracy, then Rule 11's reasonable inquiry mandate is meaningless.

D. The District Court Exercised Discretion Consistent With Its Power Under The Rules Enabling Act

The proceedings below are devoid of any challenge to the amount of sanctions imposed on Business Guides.

Now Business Guides joins Amicus[14] in arguing that the premise of awarding sanctions in the amount of attorney fees is a form of fee shifting and as such beyond the grant of power of the Rules Enabling Act[15] under the reasoning of *Alyeska Pipeline Service Co. v. Wilderness Society*, 421 U.S. 240, 44 L.Ed.2d 141 (1975). Its reliance on *Alyeska*, however, is misplaced.

In *Alyeska*, this Court rejected the judicial creation of a prevailing party's right to attorney fees under a private attorney general concept, where no statute authorized the award. To violate the Rules Enabling Act, under the reasoning of *Alyeska*, Rule 11 would have to mandate an award of full attorneys' fees to the prevailing party. It does not. Rule 11, like other federal procedural rules,

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[14] Amicus, Public Citizen, is a consumer advocacy group. One presumes that to further its cause of consumer protection it sometimes advocates creative interpretation and application of the law. It may also be the case that when it files suit against an entity such as a manufacturer, most of the evidence it will ultimately require to prove its case will have to be discovered from defendant. Although not stated, respondents assume that it fears having to pay attorney fees if its creative view of the law is rejected and discovery ultimately renders its claim groundless. Affirming the Ninth Circuit here does not lead to such a result. This is not a case where the litigant was sanctioned for advocating a creative view of the law or where later-discovered evidence proved the claim unfounded. Rather, it involves abuse of an established practice in copyright law in which all of the discredited evidence was in the hands of the sanctioned party.

[15] The Rules Enabling Act states: "(a) The Supreme Court shall have the power to prescribe general rules of practice and procedure; . . . (b) Such rules shall not abridge, enlarge or modify any substantive right." 28 U.S.C.A. § 2072.

including Rule 37, lists the award of a "reasonable attorney's fee" as one possible sanction, but leaves the choice of the most appropriate sanction to the sound discretion of the trial court. Business Guides was not sanctioned because it was not a prevailing party. It was sanctioned because it violated Rule 11 by failing to conduct a reasonable inquiry before filing a specious copyright infringement action. This Court recently observed that the central purpose of Rule 11 is to deter baseless filings in District Court. So long as courts enforce the Rule consistent with that purpose, it will be consistent with the Rule Enabling Act's grant of authority to streamline the administration and procedure of the federal courts. *Cooter & Gell* at 374.

The District Court in this case acted in accordance with the terms of Rule 11 to achieve its primary purpose of deterrence. It dismissed the lawsuit, having found, after multiple evidentiary hearings, that the evidence upon which it rested was entirely erroneous. Then, consistent with Rule 11's goal of deterring frivolous suits and needless consumption of court time, it imposed monetary sanctions against the party responsible in an amount equal to the cost to Chromatic in attorneys' fees. Conceivably it was within the Court's power to impose additional sanctions to compensate the court, and indirectly the public, for the innumerable hours wasted because Business Guides failed to devote an hour to verify its evidence. Under the circumstances, the Court exercised considerable restraint. Because the district court acted pursuant to the express terms of the Rule to achieve its legitimate procedural purpose, the sanctions award was well within its power under the Rules Enabling Act.

CONCLUSION

For all the foregoing reasons, the decision below should be affirmed.

Dated: September 20, 1990

Respectfully Submitted,

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